

countries, including several in the Middle East that are not on the list have nonetheless had problems in implementing the recommendations. The FATF could ask member countries to implement sanctions against black listed countries but has so far refrained from this choosing instead to work with countries that have yet to meet the required standards. (Jonathan M. Winer and Trifin J. Roule, "Fighting Terrorist Finance," *Survival*, vol. 44, no. 3, August 2002.)

46. The FATF has also issued a self-assessment questionnaire concerning observance of the eight recommendations to both FATF and non-FATF members and considers the response at review meetings. Countries and territories on the FATF's list have generally worked with the FATF to improve their anti-money-laundering systems. Member governments have promised to provide assistance to non-members to help them comply with the FATF's special recommendations.

47. The International Monetary Fund has recently extended its mission beyond its voluntary Financial Sector Assessment Programme and a separate programme to assess offshore financial centres. Its anti-money laundering work now incorporates legal and institutional frameworks, undertakes onshore assessments, helps member countries identify gaps in their enforcement systems and provides technical assistance to enable members to implement the agreed international standards. IMF assessments now use the criteria contained in the FATF's 40 principles for the proper administration of financial centres. The Fund has resisted calls to take on enforcement functions, arguing that this would exceed its mandate. (IMF Survey, November 26, 2001.) The IMF's Financial Committee, however, has called on all member countries to establish financial intelligence units to investigate reports of suspicious transactions, monitor suspected terrorist funds and develop ways to share information. The IMF is scheduled to give a progress report on its efforts at its 2002 Annual Meeting. The IMF assessments provide a road map for plugging gaps in systems that criminals and terrorists have been able to exploit. The UK, in partnership with Canada, the World Bank and the IMF for example, has established the Caribbean Regional Technical Assistance Centre (CARTAC) in Barbados to strengthen the region's financial sector. This spring the World Bank/IMF, the UK, Canada and Switzerland launched a US\$45 million Financial Sector Reform and Strengthening Initiative (FIRST) to assist low and middle-income countries in short and medium term capacity building and policy development.

48. One serious drawback in all these programmes is that they focus on national efforts to contain money laundering rather than on the standards and practices of individual banks and financial firms. Although the 11 largest global banks have developed the so-called "Wolfsberg Principles" that established basic "know your customer" and due diligence standards, there has been no comprehensive effort to certify institutions that have implemented best practices globally. Governments, for example, find it exceedingly difficult to exercise full control over foreign subsidiaries of national banks. This may be an area where international financial institutions could help in providing certification. Even before the attacks, a US Senate sub-committee on investigations said weak control over correspondent banking had created a gateway for rogue foreign banks to launder cash. (John Willman, "Cleaning up", *Financial Times*, September 21, 2001.) But the American banking industry and its Congressional supporters initially blocked efforts to give the Treasury Secretary power to bar foreign countries and their banks that did not cooperate with money laundering investigations from access to US financial markets. (Tim Weiner, David Cay Johnston, "Bin Laden's Money Trail is littered with U.S. investigators mistakes", *International Herald Tribune*, September 21, 2001.) US views on this have shifted since September 11.

49. One suggestion now on the table would have the UN lead a push for global adoption of "know your customer" rules and other anti-money laundering policies in banks and branches followed by publicised assessments of compliance. Those banks that pass muster would then be approved for dealing with funds of international organisations like the World Bank, the IMF and national governments. Although this initiative would not directly concern problem banks that have no dealings with public money, it would begin to make sharper distinctions between helpful and unhelpful banks and could encourage the private sector to reward those banks that are effectively "white listed". (See Jonathan Winer, "Illicit finance and global conflicts, Programme for International Cooperation and Conflict Resolution", Fafo Report 380, www.fafo.no/pub/rapp)

VI. DEVELOPMENT AID

50. Development aid represents yet another economic aspect of the Western response to the attacks. Obviously it would be a mistake to characterise international development assistance as little more than a tool of anti-terrorism. To do so would diminish its role in assisting underdeveloped countries in achieving greater levels of prosperity and political stability. Yet, granting development assistance is at once an act of solidarity and of self-interest, and of course, economic and political development are likely to be helpful in addressing some of the conditions that certain terrorist groups have ably positioned themselves to exploit.

51. Development policy has recently been the subject of a certain amount of transatlantic friction. In some US political and economic circles, development aid has been characterised as little more than a source of corruption and market distortion generating more problems than it solves. This view has gathered some momentum in the United States, and aid spending has declined rather dramatically in recent years. Jeffrey Sachs recently noted, "American aid is 0.1% of GDP, a derisory shadow of what it used to be and roughly one third of the European level." ("What's good for the poor is good for America," *The Economist*, July 12, 2001.) Indeed, European governments give a higher percentage of GNP to foreign assistance programmes and are sometimes critical of the low levels of US contribution. They also argue that spending has grown more effective as international donor institutions increasingly focus their efforts on the supply-side and particularly on market and state institution building programmes. In recent months, moreover, Europeans have expressed some frustration with a US proposal that half of World Bank aid to the poorest nations takes the form of grants instead of low-interest loans. The Europeans are worried that this will empty the Bank's reserves, which might not then be refilled. (Michael M. Phillips, "U.S.

Treasury Chief vigorously defends foreign aid policy", Wall Street Journal, February 22-24, 2002.) The Administration has denied this, responding that many World Bank loans will never be repaid anyway, so any pretence of "lending" should be dropped. Clearly there are underlying philosophical differences at play here, and it is important to conduct a dialogue to resolve these tensions.

52. At the UN Monterrey conference on development aid, the United States surprised some delegates by announcing an additional \$5 billion in annual funding. That conference hinted at a potential emerging international consensus on trade, aid, investment, debt and governance, with both developed and developing countries recognising their mutual responsibilities in dealing with poverty. Although, President Bush's increase will still leave United States near the bottom of the table in terms of aid as a percentage of GNP, a number of European observers viewed the initiative as a positive first step. (Alan Beattie, "US wakes from 20-year slumber in development field", Financial Times, March 25, 2002.) At Monterrey, President Bush insisted that new approaches are needed to ensure that funds are well spent. The Europeans feel that development strategy has been evolving in recent years, and many aid organisations like the World Bank and regional development banks have learned important lessons through post-facto project analysis. But the need for aid and active engagement grows ever more apparent. The Afghanistan case has clearly been instructive. Western neglect of that country following the withdrawal of Soviet troops created a vacuum that the Taliban and al-Qaeda ultimately filled. Policy makers now recognise that development assistance must be a critical foundation of both the US and European strategy not only in Central Asia but also in those countries where abject poverty can combine explosively with an absence of central government authority and a poisoned ideology that seeks scapegoats.

53. There are some concerns in the developing world that American and European calls to link aid to economic reform, while potentially very positive, could become simply a Western instrument to demand market opening without offering reciprocal access. That perception can only engender deeper resentment. On the other hand, opening product markets to those products in which the developing world is most competitive, including agriculture and textiles, would represent a real advance in development strategy while demonstrating that Western countries are intent on building a real economic partnership. This should remain a central theme of the Doha Round of trade negotiations.

54. Finally, there have recently been important transatlantic disagreements regarding trade strategies with countries associated with the sponsorship of terrorism. The EU, for example, recently struck a trade and cooperation agreement with Iran. Where the US Administration sees a state sponsor of terrorism, European governments observe a society in the midst of a political evolution with potentially positive implications. The EU understands trade as a way to engage the positive forces in Iranian society, a view reflecting the very same logic that the United States employs with other regimes in the world including China. This difference suggests that Western allies need to deepen the dialogue among themselves about how to engage countries like Iran.

VII. THE ROLE OF THE EUROPEAN UNION

55. While the European Union has only just begun to develop its security and defence functions, its amply developed competencies in economic policy-making, and expanding diplomatic and judicial functions have made it a central player in the anti-terrorist campaign. Last autumn's attacks clearly inspired the Union to assume a major role in the anti-terrorist struggle. But this is a challenging endeavour. Europe's governments, perhaps even more so than their American counterparts, do not see the terrorist threat as primarily military in nature. The EU has called for a broad strategy including intelligence, police, diplomatic and economic approaches in which its strengths are well evolved. That is not to say that European governments fail to recognise the important military challenge they face, but the Union's defence identity is in its infancy and member governments are still struggling to develop a capability to carry out the so-called Petersberg tasks.

56. In the wake of the September 11 attacks, Foreign Ministers agreed to make anti-terrorism a Union priority and to coordinate Europe's response. EU leaders subsequently jointly defined terrorism and froze assets of terrorist groups or those suspected of funding terrorism. Until that point, several EU nations had yet to legally define terrorism and pass a range of needed anti-terrorist legislation. EU governments have also deepened judicial and police cooperation and agreed to a common arrest warrant that should expedite extradition requests. The plan is awaiting final approval from the Italian government, which claims to have certain constitutional problems with the proposal. ("EU Crisis Response Capabilities: An Update", ICG Report, April 29, 2002.)

57. The Council of Ministers has also expanded the list of transactions covered by its money-laundering directive. Casino owners, notaries, accountants, auditors, real estate agents, and fund-transporting companies will henceforth be obliged to identify clients, adopt more stringent record-keeping norms and report suspicious transactions. (http://europa.eu.int/comm/external_relations) The Council has also vowed to take punitive action against states that refuse to adhere to international norms on combating money laundering. In December 2001, Ministers created Eurojust to coordinate cross-border investigations into crimes such as terrorism and money laundering and Europol has recently opened an office in Washington, DC to facilitate cooperation with the United States. EU governments have also set up Financial Intelligence Units as set out by the FATF to investigate and share information on money-laundering operations and potential terrorist financing.

58. It should also be noted that the EU is not taking a direct military role in Afghanistan. Yet 13 member-countries are participating in the International Security Assistance Force (ISAF), and a number of European armies, in fact, actively

supported the US campaign against the Taliban and al-Qaeda. The Union, however, has played a leading part in bankrolling Afghanistan's reconstruction. Its \$2.3 billion pledge is the largest single aid donation to Afghanistan.

VIII. CONCLUSIONS

59. In formulating a long-term response to the terrorist threat, it is essential that the remedies - tightened border controls, higher security outlays, travel restrictions, business controls etc. - not be so burdensome as to endanger economic prosperity. If our societies build walls that undermine the creation of new wealth, then the terrorists will have won an important battle. Western societies are by definition open. To revoke this openness in the name of security would be to concede victory without a struggle. New security measures are certainly essential, but these policies must be set with an eye on the fundamental values of freedom, liberal markets and free trade. This means striking a balance between greater vigilance and continued cultivation of openness.

60. Keeping trade open and free is critical to economic recovery from the shock of September 11. This is particularly the case as heightened security requirements have added new burdens to the international trading system. These are akin to a security tax; yet further trade taxation in the form of protectionism is a formula for disaster. The open transatlantic trade relationship is not only an element of solidarity, but also a foundation of prosperity. Open trade regimes are also perhaps the best way to promote economic growth in much of the world. And development, in turn, will help combat conditions that erode state authority and thus alienate citizens to the point where terrorist action is seen as legitimate by a large swathe of a given population.

61. It is essential that NATO countries review the vulnerability of crucial infrastructure to acts of terrorism and where necessary develop backup emergency systems. But these vulnerabilities raise even more profound long-term questions that cannot be ignored. To take one example, energy infrastructure is acutely susceptible to terrorist attack. This certainly requires building parallel systems, but our governments should also recognize the need to develop alternative energy sources and promote conservation. While renewable energy and conservation are often seen as a means to reduce greenhouse gases, they must also be understood as a way to enhance national security. Insofar as solar and wind power reduce dependencies on unstable regions of the world, they also increase security. A recent study estimated that it has cost the West \$100 billion to patrol the Gulf region since 1990 - the equivalent of an additional \$14 to the price of a barrel of oil in that period. ("The Terrorist crisis, A New Energy Strategy", Rusi News Brief, Vol. 21, No. 12, December 2001.) With oil prices again on the rise, the need for encouraging alternative energy production and broad energy conservation is all the more apparent and should be understood as an element of an overarching security strategy.

62. Economic aid policy must be recognised as another foundation of security strategy, although its merits obviously transcend anti-terrorism. The number of people living in poverty is climbing almost inexorably. There is little doubt that a growing gap between the few wealthy countries and the many poor ones creates conditions of political instability that can nurture extremism. Growing poverty in parts of the developing world weakens states and, in certain instances leads to a collapse of sovereign authority, leaving the door open to international criminal and terrorist organisations. Western countries must strive to close this horrific wealth gap or else face serious economic, security and indeed moral consequences. Providing aid and supporting investment and policies that will lead to sustained economic development is essential.

63. To a certain degree, the United States government has shown some renewed appreciation of this logic, and its recent announcement of an additional \$5 billion a year in foreign aid should be applauded as a positive first step. The next challenge will be to ensure greater coordination of aid programmes between the US, the EU and the international community at large. It is also essential that the West dedicate itself to rebuilding Afghanistan. Afghanistan was abandoned to its own fate after the withdrawal of the Soviet Red Army, and it became a magnet for terrorists as well a global supplier of opium. The West must offer strong and sustained support to the Afghan government and its people to avoid a repeat of this tragic cycle.

64. Greater international cooperation is essential to countering money laundering and terrorist financing. The work of the Financial Action Task Force has been particularly helpful in setting standards for national regulators, and will continue to be the lynchpin of this effort. More work is needed to introduce "know your customer" and due diligence rules to all banks operating internationally. This requires greater collaboration not only with national regulators but also with the banks themselves. It might make sense not only to publicly acknowledge countries that are not fully compliant with agreed standards but also institutions implicated in money laundering. This would combine the principles of universal private sector self-regulation with the strategy of standard setting and list publishing that both the OECD and the FATF employ. It has also been suggested that international organisations and governments only conduct business with those financial institutions with a clean bill of health. A higher degree of legal harmonization in the area of banking law would promote stronger international regulation, while a dialogue between bankers and regulators can determine which rules work in tracking down terrorists and which do not. Finally states that do not comply with the FATF recommendations must be offered incentives to do so. All manner of support should be extended to those states that are genuinely disposed to align themselves with international norms while strict sanctions will ultimately be needed to penalize those that do not. A great deal has been accomplished on this front over the past year with jurisdictions from the Channel Islands to Liechtenstein adopting far more stringent controls; but more can be achieved notably in the Gulf region. Securities regulators must tighten rules to prevent the misuse of equity markets by terrorist financiers. It would also be helpful to highlight the efforts of individual banks to implement stringent "know your customer" rules and defend their global operations from terrorist exploitation.

65. According to a recent UN Report, it is also necessary to apply stricter controls on hawalas as well as religious charities, several of which are suspected in bankrolling al-, Qaeda, and consider removing some of the evidentiary standards that have made it difficult to seize individual assets of suspected terrorists. At the same time, our governments should strengthen conventional wire systems for customers (normally migrant workers) who are often unwilling to pay large fees on very small regular amounts sent home.

66. In order to retain relevance as the foundation for its members' security, NATO must now develop and refine its anti-terrorist capabilities. It cannot do so without considering the economic dimensions of the threat. NATO itself cannot play an operational role in matters like money laundering and asset seizure, but it is vital that it develop the capabilities to monitor developments in these areas because they are, in a certain sense, the key to the "defence budgets" of terrorist groups. ("NATO's Economic Dimension after Rome and Prague", remarks by Patrick Hardouin to the NATO PA Economics and Security Committee, May 24, 2002.) Nor can the Alliance ignore the financial activities of sub-state actors including terrorists involved in weapons proliferation. Actively monitoring developments in these areas should become a central element of NATO threat assessments.

* Cook Islands, Dominican Republic, Egypt, Grenada, Guatemala, Indonesia, Marshall Islands, Hungary, Israel, Lebanon, Marshall Islands, Myanmar, Nauru, Nigeria, Niue, Philippines, Russia, St. Kitts and Nevis, and St. Vincent-Bulletin Quotidien Europe, No 8240 June 24, 2002.

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